

# **TECHNICAL ASSISTANCE – DIFFERENT COMPONENTS OF INDEPENDENT CONTRACTING**

Prepared by the Division of Human Resources in the Department of Personnel & Administration. Revised November 2005.

## **GENERAL**

There are two major considerations when determining permissible independent contracting: first, whether the relationship is an independent contractor; and second, if state law permits the contract. When it comes to determining who is an independent contractor, the following are general guidelines and best practices for managing independent contractors. This information is drawn from case law, IRS guidance, and other policies on independent contracting and is designed to assist departments with properly establishing independent contractor relationships for tax and other regulatory compliance even if the contract is appropriate under Part 5 of title 24, article 50. In addition, please refer to the chart to help with differing types of independent contractors or leased workers scenarios. As one of the central approvers, the Division of Human Resources (DHR) applies the statute in light of these guidelines.

There are two general types of independent contracting agreements. One is an agreement directly with an individual (i.e., sole proprietor). The other is to obtain a “leased worker” indirectly through another company, e.g., Job Store, which these guidelines refer to as a Multi-Employee Contractor or Company.

In determining an independent contractor versus an employee, a couple of questions should be answered. The crucial one being, what is the relationship? Does the contracting department control the means and the method for accomplishing the tasks or is the individual sufficiently independent from the contracting department and its control? Once the relationship has been determined, departments must also establish if the independent contract is permitted under the civil service amendment and associated statutes and rules.

There can be differences in the degree of control over the work based on the nature of the relationship. In all cases, there should be clearly defined end results or deliverables with specified deadlines or due dates. In addition, the following should be considered in all independent contract relationships. Does the worker:

- determine his or her own work schedule;
- freely work for several other clients;
- have his or her own place of business;
- use his or her own equipment; and,
- bill by an hourly rate, or lump sum for specified deliverables.

In addition to the above, federal law looks at:

- the amount of investment in facilities and equipment relative to your investment;
- the amount of skill, initiative, judgment, or foresight required for the worker to succeed;
- the workers independence in the structure of the business organization and operation; and,
- the permanency of the relationship between the business and the worker.

These factors alone are not sufficient to determine worker status. The law requires examination of the substance of the relationship in totality and a determination of where the weight falls, independent contractor or employee. Regulators will look at what is actually occurring, not merely what is contained in the contract. All labor relationships are presumed to be employment relationships so contracting departments have the burden of demonstrating otherwise, if challenged. In addition to the statutes on personal services contracting, other state law provides some guidance on what to include in independent contracts (refer to CRS 8-40-202 on workers compensation and CRS 8-70-115 on unemployment benefits).

### **Multi-Employee Contractor**

An employment agency or firm (“company”) assigns identified individuals to carry out specific assignments, e.g., data entry, clerical, IT services (leased workers). The relationship is with the company itself, not the leased worker assigned to perform specific duties. These individuals are employees of the company and, as the primary employer, the company is responsible for all employment-related functions, including those required by federal and state laws, e.g., performance reviews, benefits, worker’s compensation, primary FMLA rights, and payroll deductions.

Under this category, it is possible that there may be a certain amount of control over the individuals performing the work, e.g., work schedule, direction on how to perform a specified service. However, it is critical that departments clearly distinguish the difference between state employees and leased workers. Courts have ruled in favor of a complainant who alleges a contractual relationship has evolved over time into an employer-employee relationship. Under the FLSA, both the company and contracting department are responsible for complying with FLSA overtime provisions and if there is a violation, both could be liable. A leased worker has the option to sue the company, the contracting department, or both. To protect the state against liability for overtime errors made by the company, the contracting department must accurately report any overtime hours worked by the leased worker to the company. In addition, a provision should be included in the contract that addresses the company assuming full responsibility for complying with the FLSA and any other state or federal employment laws.

Current state employees should not be referred to a company to perform the same work being performed for the department in order to avoid issues such as overtime payment and FTE limitations or reductions.

As a general rule, leased workers should **not**:

- repeat contracts or assignments without a six-month break between contract work, except as established by multi-year contracts;
- participate in employee functions, such as employee council, staff meetings, employee social functions;
- have offices or cubicles with their names posted similar to employees;
- have an assigned phone number that is listed in the department’s directory; and,
- receive performance recognition\* by the department instead of through the company.

\*Performance recognition includes monetary or non-monetary awards for performance and performance reviews. This does not include contract performance standards as outlined in the contract. Contract performance should be monitored and addressed as established by the contract provisions.

It is recognized that, in order to clarify service requirements, departments need to have meetings with leased workers to check project status and other related matters. In these instances, departments should call leased worker meetings to address these issues and keep regular employee staff meetings separate.

If departments require leased workers to wear badges, they should clearly identify them as such and be distinguished from employee badges. In addition, should a leased worker have issues with employment matters, such as compensation, the issue must be addressed with the company, not the state department.

### **Sole Proprietor**

This individual is self-employed, is recognized as an independent contractor by the IRS, and is responsible for paying his or her own taxes as established under federal and state law. Under this category, the department has very little control over the means or methods of how the contractual obligations are carried out. Criteria for determining independent contractors are established under state and federal law and regulations. In some cases, the individual may be required to perform specific services onsite, e.g., testing or software instruction. The specifics of when these can be performed on state property should be outlined in the contract. However, the specific steps required to get to the end result or deliverable is not specified.

### **State Personnel System Impact**

In addition to considerations of the independent contractor status, departments must also consider the impact on the state personnel system. The law gives preference to employees for long-term labor needs. In general, if there is a need for using contract workers in the same capacity for an extended period of time, the contracting department needs to assess if the labor need is an ongoing permanent requirement of the state. If the labor need is ongoing and is an integral part of the department's function, state employees should perform the work. This does not preclude contracting out a state function performed by state employees as long as any employees are not involuntarily separated from state employment as a result of the contract. This includes having a sensible plan for mitigating any impact on state employees, e.g., redeploying and retraining employees to meaningful work that retains the same base pay, status, and tenure.

### **Former Employees**

Departments should be aware that the Code of Ethics statute, C.R.S. 24-18-201, prohibits contracting within six months with former state employees under certain circumstances. DHR is not charged with enforcement and does not monitor compliance with this specific statute, so it is important to seek advice from legal counsel regarding application of the Standards of Conduct, Code of Ethics statute. However, if during its review under C.R.S. 24-50 Part 5, DHR staff identifies a potential violation of the Standards of Conduct, Code of Ethics, it will be included in the correspondence with a department.

A former employee may return as a temporary or permanent employee subject to applicable rule and law. For example, a retiree can return as an employee for 110 days following the 30-day waiting period.

If a department contracts with a retiree or a contractor who employs a retiree, the department should be aware that contributions to retirement plans might be required. Departments are responsible for contacting the appropriate retirement plan to obtain specific requirements.

Every attempt is made to keep this information updated. For additional information, refer to the *State Personnel Board Rules and Director's Administrative Procedures* or contact your department human resources office. Subsequent revisions to rule or law could cause conflicts in this information. In such a situation, the law and rule are the official source upon which to base a ruling or interpretation. This document is a guide, not a contract or legal advice.

## Independent Contractor Guidelines

**Reminder: relationship is with business entity and not the leased worker of the business!**

<div> <div>Type of contractor</div> <div>Criteria for contractor</div> </div>	Multi-employee Contractor (Company)		Sole Proprietor Business
	Firm (provides labor to achieve a particular result)	Employment agency (provides labor only)	
A. Has place of business and listing of services available to public.	No exceptions.	No exceptions.	No exceptions.
B. Selects own clients/free to work for anyone.	No exceptions.	No exceptions.	No exceptions.
C. Determines time/place where work performed.	May be set in contract.	Allowed to be set by hiring manager.	May be set in contract.
D. Provides tools and materials.	Exceptions must be in contract.	Typically provided by State.	Not unless stated in contract.
E. Does not participate in benefit programs and not covered by worker's compensation from the State as an employer.	No exceptions.	No exceptions.	No exceptions.
F. Generally does not receive regular payments and may agree to fixed price service.	May be set by contract but tied to deliverables.	Usually a \$/hour charge (including overhead) set by employment agency (not by individual).	May be set by contract but tied to deliverables.
<b>US DOL's FLSA tests (actual relationship is crucial)</b>			
1. State does not control when or how long person works, does not control how assigned tasks are accomplished. Usually paid on a "per-job" basis. Contactor retains primary control over approach to assignment.	Exceptions must be stated in contract.	State sets hours, types of tasks, & how accomplished. Employment agency is paid at end of time period; leased worker is paid by employment agency.	Exceptions must be stated in contract.
2. Worker has higher level of opportunity for gain or risk of loss.	Company bears the risk.	Employment agency bears risk and owns the employee relationship, not the State.	Contracting is not exclusive with State and individual bears risk.
3. Worker has special talents or skills that set him/her apart from in-house skills.	Generally applies.	Generally applies.	Generally applies.
4. Brings own tools/equipment to the job (not solely determinative).	Must be specified in contract.	Usually provided by the State.	Must be specified in contract.
5. Working relationship is "for a limited purpose for a limited time."	No exceptions.	No exceptions.	No exceptions.
6. Does not perform most vital services of department like deciding policies and programs.	Contractor recommends; State retains final authority.	Always true.	Always true.

**TECHNICAL ASSISTANCE  
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